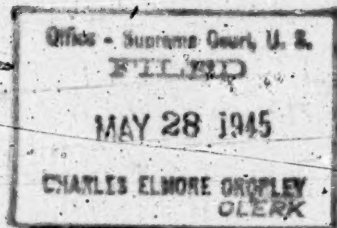


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SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1944

No. 1322 93

HERCULES GASOLINE COMPANY, INC.,

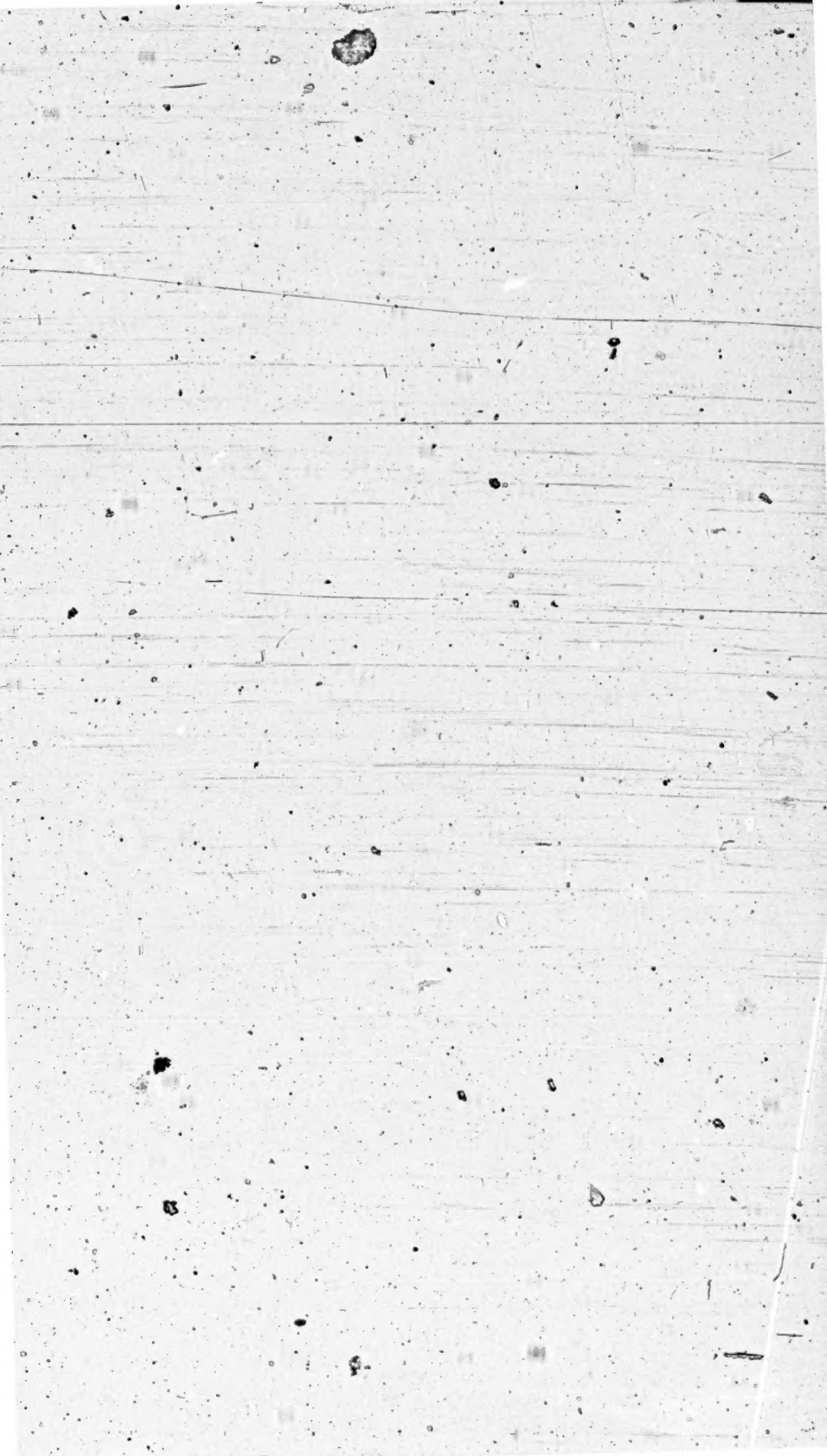
*Petitioner,*

*vs.*

COMMISSIONER OF INTERNAL REVENUE

PETITION FOR WRIT OF CERTIORARI TO THE  
UNITED STATES CIRCUIT COURT OF APPEALS  
FOR THE FIFTH CIRCUIT AND BRIEF IN SUP-  
PORT THEREOF.

MELVIN F. JOHNSON,  
*Counsel for Petitioner,*  
JOSEPH H. JACKSON,  
*Of Counsel for Petitioner.*



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**SUPREME COURT OF THE UNITED STATES**

**OCTOBER TERM, 1944**

**No. 1322**

**HERCULES GASOLINE COMPANY, INC.,**

*Petitioner and Appellant Below,*

*vs.*

**COMMISSIONER OF INTERNAL REVENUE,**

*Respondent and Appellee Below.*

**PETITION FOR WRIT OF CERTIORARI TO THE  
UNITED STATES CIRCUIT COURT OF APPEALS  
FOR THE FIFTH CIRCUIT AND BRIEF IN SUP-  
PORT THEREOF.**

*To the Honorable Harlan Fiske Stone, Chief Justice of the  
United States and the Associate Justices of the Supreme  
Court of the United States:*

Your petitioner respectfully shows:

**I**

**Summary Statement of the Matter Involved**

Section 26 (c) (1) of the Revenue Act of 1936 (26 U. S. C. A. Int. Rev. Acts, page 836) relieves corporations from surtaxes upon undistributed profits to the extent that such



profits could not be distributed without violating a provision of a written contract executed by the corporation prior to May 1, 1936, which provision expressly deals with the payment of dividends.

Petitioners transferror (a Louisiana corporation of the same name), prior to May 1, 1936, issued preferred stock certificates and incorporated therein by reference an article of its charter providing that no dividend should be paid on the common stock of the corporation until all of the preferred stock had been retired, redeemed and discharged.

The Commissioner of Internal Revenue gave notice of deficiency in income and excess profits tax for 1937, in which he claimed a surtax on undistributed profits amounting to \$32,481.53 (R. 25). Appellant filed petition to the Tax Court of the United States (R. 3), seeking a redetermination of its tax liabilities, alleging that the corporation was entitled to credit against this surtax, levied against undistributed profits by Sec. 14 of the law of 1936, by virtue of a contract between the corporation and the holders of its preferred stock which satisfied the requirements for credit under Sec. 26 (c) (1) of the tax statute. After trial, the Tax Court entered its decision upholding the Commissioner (R. 92). Petition for review was filed with the Fifth Circuit Court of Appeals, which affirmed the decision of the Tax Court, March 1, 1945 (R. 114). Thereafter, petition for rehearing was denied April 19, 1945 (R. 123).

## II

### Question Presented

The question presented is whether provisions in a corporate charter and stock certificates prohibiting the payment of dividends constitute a written contract executed by the corporation, for which the corporation is entitled to

credit against a surtax on corporate profits under Sec. 26 (c) (1) of the Revenue Act of 1936.

### III

#### **Reasons Relied On for the Allowance of the Writ**

The decision of the Circuit Court of Appeals for the Fifth Circuit (R. 114), as to whether provisions in a charter and stock certificate constitute a written contract executed by the corporation is in conflict with the decision of the Circuit Court of Appeals for the Third Circuit on the same matter in the case of *Lehigh Structural Steel Company v. Commissioner*, 127 F. (2nd) 67.

The decision of the Circuit Court of Appeals for the Fifth Circuit on this matter is likewise in conflict with the decision of the Court of Claims on the same matter in the case of *Rex Hanover Mills v. U. S.*, 53 Fed. Sup. 235 and with the decision of the Circuit Court of Appeals for the Second Circuit on the same matter in the case of *Monarch Theatres v. Helvering*, 137 F. (2nd) 588.

### IV

#### **Jurisdictional Statement**

Therefore, because of these conflicting decisions of the Circuit Courts which should be made uniform, jurisdiction is invoked under Section 240 (a) of the Judicial Code, as amended (28 U. S. C. A. 347 (a)).

### V

Your petitioner presents to this Court and files herewith as an exhibit hereto and part hereof, a duly certified transcript of the entire record in the case as the same appears in the United States Circuit Court of Appeals.

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WHEREFORE, your petitioner prays that a writ of certiorari issue under the seal of this Court, directed to the Circuit Court of Appeals for the Fifth Circuit commanding said Court to send to this Court a full and complete transcript of the record and of the proceedings of said Court had in the case numbered and entitled on the Docket No. 11,211, Hercules Gasoline Company, Inc., Petitioner, vs. Commissioner of Internal Revenue, Respondent, to the end that this cause may be reviewed and determined by this Court as provided for by the statutes of the United States; and that the judgment herein of said United States Circuit Court of Appeals for the Fifth Circuit be reversed by this Court and for such further relief as to this Court may seem proper.

Dated May —, 1945.

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Counsel for Petitioner.

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Shreveport 4, Louisiana,  
Of Counsel.



**SUPREME COURT OF THE UNITED STATES**

**OCTOBER TERM, 1944**

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**No. 1322**

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**HERCULES GASOLINE COMPANY, INC.,**

*Petitioner and Appellant Below,*

*vs.*

**COMMISSIONER OF INTERNAL REVENUE,**

*Respondent and Appellee Below*

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**BRIEF IN SUPPORT OF PETITION FOR WRIT OF  
CERTIORARI**

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*To the Honorable the Supreme Court of the United States:*

Your petitioner respectfully shows:

**1**

**Opinions Below**

The opinion of the Tax Court of the United States will be found at pages 92-102, inclusive, of the record herein.

The opinion and judgment of the United States Circuit Court of Appeals for the Fifth Circuit, including the dissenting opinion of Circuit Judge Hutcherson, is included in

the transcript of the record of that Court, attached hereto pages 114-119 inclusive. It is reported in 147 F. (2d) 972.

## II

### Jurisdiction

1. The date of the final decree of the said Fifth Circuit Court, in the case to be reviewed herein, is April 19, 1945 (R. 123).

2. The statutory provision which is believed to sustain the jurisdiction of this Court is c. 517, Sec. 6, 26 Stat. 828 as amended. (28 U. S. C. A., Sec. 347, Judicial Code, Sec. 240, amended);

“(a) In any case, civil or criminal, in a circuit court of appeals, or in the Court of Appeals of the District of Columbia, it shall be competent for the Supreme Court of the United States, upon the petition of any party thereto, whether Government or other litigant, to require by certiorari, either before or after a judgment or decree by such lower court, that the cause be certified to the Supreme Court for determination by it with the same power and authority, and with like effect, as if the cause had been brought there by unrestricted writ of error or appeal.

“(b) Any case in a circuit court of appeals where is drawn in question the validity of a statute of any State, on the ground of its being repugnant to the Constitution, treaties, or laws of the United States, and the decision is against its validity, may, at the election of the party relying on such State statute, be taken to the Supreme Court for review on writ of error or appeal; but in that event a review on certiorari shall not be allowed at the instance of such party, and the review on such writ of error or appeal shall be restricted to an examination and decision of the Federal questions presented in the case.

7  
“(c) No judgment or decree of a circuit court of appeals or of the Court of Appeals of the District of Columbia shall be subject to review by the Supreme Court otherwise than as provided in this section. (Mar. 3, 1891, c. 517, Sec. 6, 26 Stat. 828; Mar. 3, 1911, c. 231, Sec. 240, 36 Stat. 1157; Feb. 13, 1925, c. 229, Sec. 1, 43 Stat. 938.)”

3. Facts, nature of the case and ruling of the courts below bringing the case within the jurisdiction provision above quoted has already been stated in the preceding petition under I (page 1) which is hereby adopted and made a part of this brief.

### III

#### Statement

1. The corporation had a provision in its charter, which was brought into the preferred stock certificates by specific reference, reading as follows: “The common stock shall be subject to the prior rights of the holders of the preferred stock as above declared and there shall be no dividend on the common stock until all of the preferred stock has been retired, redeemed and discharged.” (R. 9). The corporation, in 1933 and 1935 had issued and in 1937 had outstanding 1294 shares of the par value of \$50 per share, the total issue thus being \$64,700. There is no dispute as to the facts, no contest as to transferee liability no denial concerning the issue of this stock, nor that it was issued prior to May 1, 1936 or that it expressly deals with the payment of dividends. The Commissioner first raised the point in his 90 day letter that the preferred stock certificates do not constitute a “written contract” within the meaning of Sec. 26 (c) (1) of The Revenue Act of 1936 (R. 23).

2. Act 250 of the Legislature of Louisiana of 1928, Sec. 14, specifically authorizes rights and restrictions concerning

preferred stock to be incorporated into the certificates by reference to the charter. The taxpayer observed this law by referring to the charter in both the preferred and common stock certificates. The preferred stockholders were different from the common stockholders.

3. The Tax Court sustained the Commissioner and held that these facts do not amount to "a written contract executed by the corporation" restricting the payment of dividends within the meaning of Sec. 26-(c) (1) of The Revenue Act of 1936 (R. 99-100).

4. The U. S. Circuit Court of Appeals for the Fifth Circuit affirmed the Tax Court, disallowing the credit claimed under the contract restriction (R. 114 et seq.), giving a different basis for decision than had the Tax Court. The Circuit Court gave as its opinion that the question had been answered by this Court in the case of *Helvering v. Northwest Steel Mills*, 311 U. S. 46. In a strong dissenting opinion, Circuit Judge Hutcheson criticized the majority opinion and stated that he thought the taxpayer herein was entitled to the credit he claimed and that the judgment of The Tax Court was wrong (R. 117-119).

5. The Circuit Court of Appeals for the Third Circuit in 1942, 127 F. (2nd) 67, concluded that stock certificates containing similar provisions to those issued by Hercules Gasoline Company did evidence a contract between the parties. See also the decision of the same court in *Budd v. Commissioner*, 143 F. (2nd) 784.

6. In similar and closely related cases in the Court of Claims (*Rex Hanover Mills v. U. S.*, 53 Fed. Sup. 235) and the Second Circuit Court (*Monarch Theatres v. Helvering*, 137 F. (2nd) 588), the courts decided contrary to the Fifth Circuit Court ruling in the present case and thus there is what very plainly appears to be a conflict between decisions.

of the Circuit Courts and other Federal Courts which this court should review and reconcile to the ends of justice and uniformity.

#### IV

#### Statute Involved

1. The Revenue Act of 1936 (26 U. S. C. A. Int. Rev. Acts, page 835) levied a surtax on undistributed profits commencing at 7% and going to 27% on the adjusted net income. Section 26 of this Act allows certain credits against the tax, as follows:

#### Sec. 26. Credits of Corporations:

In the case of a corporation the following credits shall be allowed to the extent provided in the various sections imposing tax—

#### (c) Contracts Restricting Payment of Dividends.

(1) Prohibition on payment of dividends. An amount equal to the excess of the adjusted net income over the aggregate of the amounts which can be distributed within the taxable year as dividends without violating a provision of a written contract executed by the corporation prior to May 1, 1936, which provision expressly deals with the payment of dividends. If a corporation would be entitled to a credit under this paragraph because of a contract provision and also to one or more credits because of other contract provisions, only the largest of such credits shall be allowed, and for such purpose if two or more credits are equal in amount only one shall be taken into account.

(2) Disposition of profits of taxable year. An amount equal to the portion of the earnings and profits of the taxable year which is required (by a provision of a written contract executed by the corporation prior to May 1, 1936, which provision expressly deals with



the disposition of earnings and profits of the taxable year) to be paid within the taxable year in discharge of a debt, or to be irrevocably set aside within the taxable year for the discharge of a debt; to the extent that such amount has been so paid or set aside. For the purposes of this paragraph, a requirement to pay or set aside an amount equal to a percentage of earnings and profits shall be considered a requirement to pay or set aside such percentage of earnings and profits. As used in this paragraph, the word "debt" does not include a debt incurred after April 30, 1936.

(3) Double credit not allowed. If both paragraph (1) and paragraph (2) apply, the one of such paragraphs which allows the greater credit shall be applied; and, if the credit allowable under each paragraph is the same, only one of such paragraphs shall be applied.

## V

### Specification of Errors

The Fifth U. S. Circuit Court of Appeals erred:

1. In holding that the provisions prohibiting dividends in the charter and stock certificates of petitioner, Hercules Gasoline Co., Inc., do not constitute a written contract executed by the corporation.

2. In holding that Your Honors in *Helvering v. Northwest Steel Mills*, 311 U. S. 46, were intending to decide that provisions in stock certificates were not written contracts executed by the corporation within the meaning of this statute.

3. In holding that 26 (c) (1) requires that the credit against undistributed profits only applies to corporations contractually obligated to set earnings aside for the payment of debts (Sec. 26 (c) (2)).

### Reasons for Granting the Writ

1. It will thus be seen that this is strictly a legal question involving the meaning of the words "written contract executed by the corporation" in the 1936 Act. The facts in the present case are almost identical with the facts involved in the cases decided by other Circuit Courts, as to the construction of the words "contract executed by the corporation." The meaning of the language used and the principles laid down by this Court in the principal case of *Northwest Steel Mills* case, decided in 1940, also is a matter about which these courts cannot agree.

2. The Fifth Circuit Court held that to entitle a corporation to the credit it was necessary that the contract concern the setting aside of earnings toward the payment of debts. Of course, this construction of the law is wrong because petitioner is relying on Sec. 26(c) (1) of the statute quoted above which allows credit for prohibition in a contract made by the corporation with anyone. It is Sec. 26(c) (2) which allows credit for contracts with creditors of the corporation for the setting aside of earnings toward the payment of debts.

3. The decision of Your Honors in the *Northwest Steel Rolling Mills* case was a legal precedent to the extent only of deciding that to entitle a corporation to the credit there must be a written contract executed by the corporation which expressly deals with the payment of dividends. There was no such contract exhibited by the taxpayer corporation in that case, where reliance was upon the provisions of the law of the State of Washington, prohibiting deficit corporations from paying dividends.

4. The Third Circuit Court, on the other hand, has held provisions in stock certificates providing for a sinking fund for the retirement of preferred stock legally constituted a "contract" between the holders of stock certificates and the corporation issuing them and gave petitioning corporations credit under the law.

Where amendment of Delaware corporation charter, accepted by stockholders and filed with Secretary of State of Delaware provided for sinking fund for retirement of preferred stock by setting aside percentage of net earnings after payment of preferred dividends and before paying other dividends, and such provision was set out in preferred stock certificates, corporation in determining undistributed profits surtax was entitled to credit for so much of profits, as corporation paid into sinking fund on ground that each certificate constituted a "contract" within statute authorizing credit for surtax purposes for profits which corporation could not distribute as dividends without violating written contract executed by corporation. Revenue Act 1936, Secs. 14, 26 (c) (1), 26 U. S. C. A. Int. Rev. Acts, pages 823, 836.

*Lehigh Structural Steel Co. v. Commissioner*, 127 F. (2nd) 67.

Where amended articles of incorporation and preferred stock certificates prohibited corporate taxpayer from paying dividends to holders of common stock until payment into sinking fund annually of an amount equal to 3 per cent. of the preferred stock, there was a "written contract executed by corporation" expressly dealing with payment of dividends which entitled taxpayer to credit to extent of sinking fund payment in computing undistributed net income. Revenue Act of 1936, Secs. 14, 26 U. S. C. A. Int. Rev. Acts, page 823.

*Budd International Corporation v. Commissioner*, 143 F. (2nd) 784.

Agreement of corporation printed on preferred stock certificates issued in 1933 requiring corporation to pro-

vide a sinking fund before payment of dividends on any class of stock other than preferred stock constituted a "written contract executed by corporation" restricting payment of dividends within statute authorizing credit for surtax purposes for profits which corporation cannot distribute as dividends without violating such a contract. Revenue Act 1936, Secs. 14, 26 (c) (1), 26 U. S. C. A. Int. Rev. Acts, pages 823, 836.

*Rex-Hanover Mills Co. v. Commissioner*, 53 F. Supp. 235.

"It is therefore, settled in this circuit that restrictive provisions in a corporate charter, by laws and certificates of stock as are present in the instant matter, constitute a written contract within Section 26 (c) (1) of the 1936 Revenue Act."

*Philadelphia Record Co. v. Commissioner*, 145 F. (2nd) 613.

Also see:

*Eljer Co. v. Commissioner*, 134 F. (2nd) 251.

*Monarch Theatres, Inc. v. Commissioner*, 137 F. (2nd) 588.

## VII

### Conclusion

A confusion and diversity has arisen. We beg the Court to consider the conflict concerning this Federal Statute which clearly exists among the Circuit Courts of Appeal on the plain question whether stock certificates containing a prohibition against the payment of dividends legally constitute a written contract executed by the corporation. Of course, the legal consequences of this conflict are that some citizens are required to pay the tax and others are relieved; some courts hold that the relationship of stockholder-corporation is not a contractual relationship and other courts hold directly to the contrary, some courts hold that Congress intended a certain kind of contract (which Congress did not

define) and other courts hold that the words used by Congress should be given their plain meaning and should be applied as written.

Therefore, under the law and the Rules of this Court (Rule 38(5)(b)) we submit that this case is one calling for the exercise by this Court of its supervisory powers by granting a Writ of Certiorari to the Fifth Circuit Court, that the decision complained against may be reviewed and determined according to law and the decisions pertaining to this question be resolved and made uniform throughout the United States.

Respectfully submitted,

MELVIN F. JOHNSON,

*Attorney for Petitioner,*

*Hercules Gasoline Co., Inc.*

JOSEPH H. JACKSON,

*Attorney of Counsel for Petitioner.*

May, 1945.

(8507)